



Memorandum

TO: HONORABLE MAYOR AND
CITY COUNCIL

FROM: Katy Allen
Larry D. Lisenbee

**SUBJECT: ESTABLISH PUBLIC WORKS
PROGRAM SUPPORT FUND**

DATE: 05-28-04

Approved

/s/

Date

RECOMMENDATION

1. Approve the establishment of the Public Works Program Support Fund in 2004-2005.
2. Include the following in the Funding Sources Resolution for the Public Works Program Support Fund:
 - a. Establish the Capital Program Support charges in the amount of \$4,510,000.
 - b. Establish the a Transfer from the Developer In-Lieu Fee Fund in the amount of \$770,544.
 - c. Establish the Division Support charges in the amount of \$371,000.
 - d. Establish the Compensated Absence in the amount of \$8,720,000.
3. Include the following in the Appropriation Ordinance for the Public Works Program Support Fund:
 - a. Establish the Administration in the amount of \$3,907,000.
 - b. Establish the Equality Assurance in the amount of \$603,000.
 - c. Establish the Other Program Support in the amount of \$770,544.
 - d. Establish the Non-Personal in the amount of \$371,000.
 - e. Establish the Compensated Time-off in the amount of \$8,220,000.
 - f. Establish a Reserve for Compensated Absence Liabilities in the amount of \$500,000.

BACKGROUND

Since 1984, the Public Works Department has distributed its administrative costs to capital projects based on the direct labor charged to the projects during the pay period. This is referred to as "Capital Redistribution." Compensated absences, such as sick leave and vacation, are also charged directly to capital projects. While these methodologies ensure that capital-related costs are assessed to capital projects, they do not allow for the most equitable distribution of costs, nor do they facilitate the development of accurate cost estimates. To address these issues, the Public Works Department initiated an effort in August 2003 to create a business model that would accomplish five major goals:

1. Equitable distribution of Public Works support services costs.
2. Accountability for project delivery costs by centralizing non-project related costs.
3. Development of a cost allocation plan that complies with the Generally Accepted Accounting Principles and legal restrictions imposed on certain funds, including their interest earnings, such as bond funds and developer in-lieu fees.
4. Provision of adequate funds for Department's non-personal needs.
5. Response to the 1997 Engineering and Inspection Costs Audit, that stipulated "*develop and propose to the City Council an alternate method to budget and account for DPW costs charged to capital projects*".

ANALYSIS

Current Distribution of Public Works Costs

The Public Works Department provides a wide range of support services to City's capital programs, including the following:

- a. *Services that benefit the City's capital programs as a whole:* Council support and liaison, capital program database, small business outreach, and standard plan & specifications upkeep.
- b. *Services that support projects directly:* contract management, labor compliance, and invoice processing.
- c. *Department's administrative functions:* budget management, employee services, and fiscal.

With the current Capital Redistribution system, the Public Works support services costs are distributed to the various capital projects each pay period based on the proportional share of the direct labor charged from project staff during that pay period. This system does not take into account the varying levels of service provided to each of the capital programs. In addition, a couple of the capital programs, most notably the Parks and Library Bond Programs, are currently not being assessed the administrative charges, even though these programs continue receiving the support services provided by the Public Works Department.

With the current system, the treatment of paid absences also presents challenges for the equitable distribution of costs. When staff takes time off, the compensated absences, including vacation, sick leave, other leaves, are charged directly to projects. This creates an inequitable system as some projects may pay for absence expenses while others may not. This problem is accentuated when an employee retires and is compensated for the accumulated vacation hours.

Another major issue with the current methodology used to distribute costs is the lack of accountability. Because the administrative costs are charged directly to projects, these costs are not aggregated for budget discussion purposes. There is also a need to establish a non-personal budget that will address the capital-related needs, rather than having these costs charged directly to projects.

Proposed Public Works Program Support Fund

The Departments of Public Works and Finance along with the Budget Office have worked collaboratively to develop an alternative methodology to assess and account for the Public Works administrative costs, compensated absences, unfunded activities, and non-personal costs. A new Public Works Program Support Fund is proposed to account for these activities. As part of the effort, the City retained a consulting firm - the Public Resource Management Group (PRMG) to develop cost allocation plans to replace the "Capital Redistribution" methodology. PRMG is expected to complete its work in early July 2004. The cost allocations plans are subject to legal review before they are put into place and they are intended to apply retroactively to fiscal years 03-04 and 04-05. It is anticipated that the cost allocation plan will enable staff to apply a "Capital Program Support" rate to each capital project that receives Public Works' services and support.

The funding source of the Public Works Program Support Fund would be various capital funds except for a transfer (\$770,544) from the Developer In-Lieu Fee Fund. The proposed Public Works Program Support Fund does not increase any costs or change any existing funding sources. The implementation of the fund is not expected to have any net financial impact on the various capital programs or the Developer In-Lieu Fee.

This fund is comprised of five appropriations and a reserve, as described below.

1. Administration

This allocation would fund most of the personal and non-personal costs of the Public Works Director's Office and Administration Division. The Department's centralized non-personal needs: equipment, software, recruitments and training, etc., are also included. Funding for this appropriation would be supported by the Capital Program Support. The amounts transferred from the various capital funds would be based on the allocation developed by the Public Resource Management Group.

It should be noted that as the changes in this memo were developed, the Public Works Department reexamined the administrative staffing level and aligned it with the current service demands. As a result, five positions are recommended for elimination and one position for redeployment as part of the Proposed Operating Budget.

2. Equality Assurance

The Office of Equality Assurance audits the labor compliance of construction projects. This allocation would provide the funding for these construction-related audits and would be funded by the Capital Program Support.

The other functions related to the Equality Assurance will continue to be funded by their existing funding sources, such as Airport, Housing, Redevelopment Agency, and the General Fund. The Capital Program Support developed by the Public Resource Management Group would not charge any allocation to such funds as those have provided direct funding.

3. Compensated Time-off

This appropriation would account for Public Works Department's vacation, sick leave, executive leave, retirement vacation pay-off, as well as 15 holidays. With this appropriation, staff's time-off will no longer be charged directly to project and project managers will be able to manage project delivery costs more effectively. To fund this allocation, a fixed rate would be applied to direct labor when staff is working on a project, as opposed to taking time-off. Every project will pay for its fair share of compensated absence regardless of the timing of the leaves.

4. Other Program Support

The appropriation provides funding for unfunded activities and bond program support that are not eligible for reimbursements. This appropriation is funded by a transfer from the Developer In-Lieu Fee Fund and, therefore, will not financially impact other capital programs.

The transfer of interest earnings from the Developer In-Lieu Fee Fund is to reimburse a portion of the Department's administrative staffing and support that has been required to implement and maintain the Developer In-Lieu Fee Program in accordance with the Mitigation Fee Act since January 1, 1989. These costs of administration were never included in the in-lieu fees collected by the City from developers. The City is now appropriately accounting for and reimbursing itself the administrative costs of the in-lieu fee program from the interest earned on the in-lieu fees account.

5. Non-Personal

The augmentation will support the divisions' non-personal needs. Non-personal expenses such as supplies, training, professional membership, are directly charged to individual projects. With this allocation, each division's non-personal expenses will be equitably distributed among all projects within the division. Various capital funds that support these projects would fund these costs.

6. Reserve for Compensated Absence Liabilities

Because Public Works staff has accumulated vacation and sick leave hours, there is a compensated absence liability. A reserve would be established to allow the gradual building of a cash balance to address this outstanding liability. The funding source is the Compensated Absence that would be funded by transfers from the individual capital funds according to direct labor charges.

The establishment of the Public Works Support Fund will address each of the goals established for developing a new business model. This new fund will provide a more equitable distribution of costs and will provide more accountability. This new fund will also address the recommendation in the 1997 Engineering and Inspection Costs Audit; specifically, a clear picture of how the City's capital funds are used would be provided, and the Public Works' administration costs and the direct project delivery costs would be segregated.

The new fund structure is also in alignment with other jurisdictions. Staff has surveyed five of the largest cities in California: San Francisco, Oakland, San Diego, Long Beach, and Sacramento. The survey result concluded that all five cities exclude compensated absences from direct project charges and most of these cities utilize an operating fund to account for Public Works' administrative costs.

COST IMPLICATIONS

The implementation of the Public Works Program Support Fund will not impact the Proposed 2004-2005 Capital Budget or the 2005-2009 Capital Improvement Program. These costs have already been programmed as part of the individual capital project budgets.

COORDINATION

This memo is coordinated with the Office of Attorney and the Finance Department.

/s/
KATY ALLEN
Director, Public Works Department

/s/
LARRY D. LISENBEE
Budget Director

PUBLIC WORKS PROGRAM SUPPORT FUND (150)

STATEMENT OF SOURCE AND USE OF FUNDS

	<u>2002-2003 Actual</u>	<u>2003-2004 Adopted</u>	<u>2003-2004 Modified</u>	<u>2003-2004 Estimate</u>	<u>2004-2005 Proposed</u>
SOURCE OF FUNDS					
Beginning Fund Balance	n/a	n/a	n/a	n/a	0
Transfers					
Capital Program Support	n/a	n/a	n/a	n/a	4,510,000
Compensated Absence	n/a	n/a	n/a	n/a	8,720,000
Division Support					371,000
Interest - Developer's Fee Fund	<u>n/a</u>	<u>n/a</u>	<u>n/a</u>	<u>n/a</u>	<u>770,544</u>
Total Transfers	<u>n/a</u>	<u>n/a</u>	<u>n/a</u>	<u>n/a</u>	<u>14,371,544</u>
TOTAL SOURCE OF FUNDS	<u><u>n/a</u></u>	<u><u>n/a</u></u>	<u><u>n/a</u></u>	<u><u>n/a</u></u>	<u><u>14,371,544</u></u>
USE OF FUNDS					
Expenditures:					
Compensated Time-off					8,220,000
Other Program Support	n/a	n/a	n/a	n/a	770,544
Department Operating:					
Administration	n/a	n/a	n/a	n/a	3,907,000
Equality Assurance	n/a	n/a	n/a	n/a	603,000
Non-Personal	<u>n/a</u>	<u>n/a</u>	<u>n/a</u>	<u>n/a</u>	<u>371,000</u>
Total Expenditures	<u>n/a</u>	<u>n/a</u>	<u>n/a</u>	<u>n/a</u>	<u>13,871,544</u>
Ending Fund Balance					
Reserve for Encumbrances	n/a	n/a	n/a	n/a	0
Reserve for Compensated Absence Liabilities	n/a	n/a	n/a	n/a	500,000
Reserve for Equipment Depreciation	n/a	n/a	n/a	n/a	0
Restricted: Prior Year Adj.	<u>n/a</u>	<u>n/a</u>	<u>n/a</u>	<u>n/a</u>	<u>0</u>
Total Ending Fund Balance	<u>n/a</u>	<u>n/a</u>	<u>n/a</u>	<u>n/a</u>	<u>500,000</u>
TOTAL USE OF FUNDS	<u><u>n/a</u></u>	<u><u>n/a</u></u>	<u><u>n/a</u></u>	<u><u>n/a</u></u>	<u><u>14,371,544</u></u>